

The Meeting of the Advisory Committee on Community Banking
of the
Federal Deposit Insurance Corporation
Held in the Board Room
Washington, D.C.

Open to Public Observation via Webcast

October 26, 2022 - 9:00 A.M.

The meeting of the Federal Deposit Insurance Corporation (FDIC) Advisory Committee on Community Banking (Committee) was called to order by Martin J. Gruenberg, Acting Chairman, FDIC Board of Directors.

Committee members in attendance: Mike Bock, CEO, Dairy State Bank, Rice Lake, Wisconsin; Troy Campbell, President and CEO, Altoona First Savings Bank, Altoona, Pennsylvania; Anthony Capobianco, President and CEO, American Community Bank, Glen Cove, New York; Harold "Hal" Horvat, President, CEO and Chairman, Centreville Bank, West Warwick, Rhode Island; Robert James II, Executive Vice President, Carver State Bank, Savannah, Georgia; Betsy Johnson, President and CEO, Solutions Bank, Forreston, Illinois; Cynthia "Cindy" Kitner, President and CEO, Jefferson Security Bank, Shepherdstown, West Virginia; Bruce Lowry, President and CEO, Ireland Bank, Malad City, Idaho; Trey Maust, Executive Chairman, Lewis & Clark Bank, Oregon City, Oregon; Neil McCurry Jr., Sarasota and Manatee County Market President, Seacoast National Bank, Stuart, Florida; Dominik Mjartan, President and CEO, OPTUS Bank, Columbia, South Carolina; Gilbert Narvaez Jr., President and CEO, Falcon International Bank, Laredo, Texas; Arlen Osterbuhr, Chairman and CEO, Minden Exchange Bank and Trust Company, Minden, Nebraska; Shane Pilarski, President and CEO, Alliance Bank, Francesville, Indiana; Kim Reigelsberger, President, Preferred Bank, Rothville, Missouri; Andrew West, President and CEO, Eagle Bank, Polson, Montana; and John "PJ" Wharton V, President and CEO, Yampa Valley Bank, Steamboat Springs, Colorado.

Margaret Oldner, CEO, Stone Bank, Mountain View, Arkansas, was absent from the meeting.

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Michael J. Hsu, FDIC Director (Acting Comptroller of the Currency), also attended the meeting.

FDIC and FDIC contractor staff in attendance: James L. Anderson, Tawanta L. Brinson, Rhonda L. Campbell, Jermain Cunningham, Timothy J. Davin, Debra A. Decker, Doreen R. Eberley, Sheila R. Finlayson, G. Chris Finnegan, Shannon N. Greco, Patricia S. Gurneau, Daniel S. Hoople, Rosilyn L. King, M. Anthony Lowe, Thomas F. Lyons, Jonathan N. Miller, Shayna Olesiuk, Jason A. Pan, Mark E. Pearce, Nikita Pearson, Harrel M. Pettway, Ariana L. Rambuyan, Lisa K. Roy, Betty J. Rudolph, Camille C. Schmidt, Michael Shaheen, James P. Sheesley, Michael E. Spencer, Derek R. Swanson, Mona L. Thomas, Allen Yarbrough, and Katrice L. Yokley.

Acting Chairman Gruenberg opened the meeting and presided over the proceedings. Doreen R. Eberley, Director, Division of Risk Management Supervision (RMS) and the Committee's Designated Federal Officer, moderated the proceedings.

Introductory Remarks

Acting Chairman Gruenberg noted the Committee's return to in-person meetings and remarked on several macroeconomic factors currently affecting the banking industry. He and Director Hsu expressed their interest in hearing the perspectives of the Committee members.

Discussion of Banking Conditions

Ms. Eberley introduced Shayna Olesiuk, Deputy Director, Division of Insurance and Research (DIR) and Camille Schmidt, Section Chief, RMS, to provide an overview of banking conditions with particular emphasis on market, liquidity, and credit risks. Ms. Eberley invited the members to provide their thoughts on these risks and others. Members provided remarks on a variety of topics, including employee hiring and retention, liquidity risk, inflation, interest rate risk, agriculture, real estate, commercial lending, and underwriting standards.

Employee Hiring and Retention

Members reported challenges hiring and retaining qualified employees. Member Maust observed that the labor force participation rate is considerably less than it was prior to the

pandemic, which may reflect a structural change. Member Mjartan discussed the challenge of larger banks recruiting staff from community banks. Members Johnson, McCurry, and Wharton remarked on the impact of employee shortages on both banks and businesses. Members Bock, James, and Kitner emphasized the cybersecurity and regulatory risks posed by inexperienced staff and staff working remotely.

Liquidity Risk

Members expressed varying levels of concern with respect to liquidity risk. Member Campbell indicated that his bank is limiting loan participation investments to ensure his bank has sufficient liquidity to support its direct customers. Members James and Mjartan emphasized the unique liquidity challenges faced by community banks operating in underserved communities. Member Mjartan suggested that, among other things, reform of the Community Reinvestment Act may help address liquidity challenges for smaller banks.

Several members discussed increased competition for deposits. Member Campbell noted that Federal Home Loan Banks (FHLB) are the primary contingency liquidity plan for community banks and expressed concern about limited borrowing capacity.

Inflation

Members described the impact of rising inflation on community banks. Member Mjartan emphasized the uniquely strong impact of inflation on customers in underserved communities. Member Johnson expressed the concern about the impact of inflation on small businesses. Member Maust warned of potential reductions in consumer spending, and Member Wharton remarked that rising inflation exacerbates other challenges facing community banks, including housing availability and employee retention.

Interest Rate Risk

Members discussed the impact of rising interest rates, including certain actions their banks are taking in response. Members also noted the impact that rising rates have on the net interest margin.

Agriculture

Several members remarked on recent trends in the agricultural sector that have impacted community banks. Members Johnson, Osterbuhr, and Reigelsberger commented on agricultural growth following several years of good harvests and favorable prices. Member Osterbuhr indicated his bank has increased liquidity due to three years of strong performance in agriculture, which results in lower loan demand by farmers. He also noted higher agriculture costs. Member Reigelsberger observed that although grain prices and fertilizer prices are higher, profit margins remain about the same for farmers. Member Pilarski reported declines in agricultural loans as farmers paid down lines of credit following profitable years and community banks compete with the Farm Credit Administration.

Real Estate and Housing Costs

High housing costs were also a topic of member discussion. Members noted that lower housing supply and rising interest rates are impacting home purchases in many communities. Member West warned of the potential for a precipitous decline in real estate values over the next couple of years, and Member Kitner shared her concern about inflated real estate values.

Member West predicted a drop in loan demand for commercial real estate and observed increased demand for home equity lines of credit. Member Kitner indicated that due to increased volumes of work and supply chain issues, many construction loans are running longer than expected.

Commercial Lending

Members discussed commercial lending activity, describing a challenging environment for businesses amid inflation, rising interest rates, and labor shortages. Member James expressed concern about small business lending.

Underwriting Standards and Portfolio Stress Testing

Members discussed whether changing economic conditions had necessitated adjustments in underwriting standards among community banks. Members Capobianco, Horvat, Kitner, McCurry, Osterbuhr, and Pilarski indicated that their institutions had not adjusted underwriting standards. Member Horvat observed that one positive trend is that competing banks have not changed

their underwriting standards. Member West indicated his bank made some underwriting changes to protect against potentially declining home values. Members Capobianco, West, and Osterbuhr reported that their institutions were stress testing their portfolios, while Member Kitner suggested that the long-term rising rate environment posed challenges in establishing meaningful benchmarks for stress testing.

At the conclusion of this discussion, the meeting stood in recess from 10:32 a.m. to 10:50 a.m.

Update from the Minority Depository Institutions (MDI) Subcommittee

The proceedings resumed with Ms. Eberley introducing Committee Member Narvaez, a member of the MDI Subcommittee, as well as Betty Rudolph, Director, Office of Minority and Community Development Banking. Ms. Rudolph began by providing background details about the purpose, goals, and composition of the MDI Subcommittee.

Member Narvaez provided a summary of the discussion topics from the two meetings held by the MDI Subcommittee in 2022. He indicated that the MDI Subcommittee had no current recommendations for the FDIC. Member James shared remarks about risks associated with rapid growth due to the recent influx of capital into MDIs. He inquired about technical assistance the regulatory agencies could provide relative to prudent management of MDI asset growth. Ms. Rudolph shared some details about a technical assistance effort that is currently being piloted. Acting Chairman Gruenberg encouraged MDI community bankers to stay in close contact with their regulators for support and technical assistance in managing the risks associated with the capital influx. Member James also highlighted the importance of tailoring the FDIC examination process to the unique mission and role MDIs serve in their communities. Ms. Rudolph shared information regarding just-in-time training that the FDIC is rolling out.

Amended Restoration Plan and Deposit Insurance Assessments

Ms. Eberley introduced Michael Spencer, Associate Director, DIR, and Daniel Hoople, Section Chief, DIR, for a presentation regarding the Amended Restoration Plan and deposit insurance assessments.

At the conclusion of the presentation, Mr. Hoople and Mr. Spencer answered questions from Members Johnson and Mjartan pertaining to potential changes to the deposit insurance limit and the analysis that formed the basis for the planned assessment increases. Acting Chairman Gruenberg remarked on the importance of maintaining the proper reserve ratio and pointed out that the planned assessment increase could prevent a later increase during a time of potentially greater economic difficulty.

At the conclusion of this discussion, the meeting stood in recess from 11:29 a.m. to 1:06 p.m.

Supervision and Policy Updates

The meeting resumed with Ms. Eberley leading a discussion of various supervision and policy updates. First, Ms. Eberley and G. Chris Finnegan, Senior Deputy Director, Division of Depositor and Consumer Protection (DCP), discussed the FDIC's return to on-site bank examinations.

Members generally supported a hybrid examination format including both on-site and remote elements. Members Campbell, Lowry, Mjartan, and Reigelsberger remarked that having examiners on-site added significant value to the examination process. Members Lowry, Mjartan, and James also expressed concern about the logistical burden imposed on community banks by large examination teams. Several members recommended that the FDIC strike a balance between remote and on-site examination work, with on-site examiners focused on high-risk items and portions of the examination process that do not translate well to remote work. Members also discussed potential opportunities to streamline the examination planning process.

Mr. Finnegan then provided an overview of a Financial Institution Letter regarding the assessment of multiple non-sufficient funds fees for the re-presentment of unpaid transactions. He also discussed the fees associated with "Authorized Positive/Settle Negative" transactions.

Ms. Eberley next introduced Jonathan Miller, Deputy Director, DCP, and Rhonda Campbell, Senior Attorney, Legal Division. Mr. Miller and Ms. Campbell presented information regarding the Part 328 rule concerning false advertising and misrepresentation of insured status, the FDIC portal for submitting complaints about suspected misrepresentations

regarding deposit insurance, and the Request for Information on the modernization of advertising and FDIC logos.

Members expressed concern about the risks posed by misrepresentations and customer confusion about the nature and availability of deposit insurance. Specifically, Member James remarked on the importance of establishing bright-line distinctions between banks and nonbank entities. Member Maust expressed appreciation for the active role that the FDIC has taken in combating misrepresentations regarding deposit insurance. Acting Chairman Gruenberg reiterated the commitment of the FDIC to prevent customer confusion and noted that the FDIC takes any FDIC insurance misrepresentation very seriously.

Ms. Eberley then introduced Thomas Lyons, Associate Director, RMS. He provided information regarding the proposed Interagency Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts.

Office of the Ombudsman Update

Ms. Eberley proceeded to introduce M. Anthony Lowe, the FDIC's Ombudsman, to provide an update on the Office of the Ombudsman. He described highlights from the Ombudsman's 2021 Annual Report and discussed results of recent post-examination surveys. Member Osterbuhr posed a question pertaining to capital requirements for FHLB lending and a request for the Federal Housing Finance Agency to amend the rule and change the requirement. Ms. Eberley provided additional details on the rule and corresponding restrictions on FHLB lending. She explained that for institutions that either have negative tangible equity capital or are on a path to that based on unrealized losses on available-for-sale securities, the FDIC would discuss management's strategies for funding and working through the issue. Member Johnson suggested that the regulatory agencies and FHLB work together to find a way for the FHLB to continue lending to community banks.

As Mr. Lowe's presentation was the final item for the day, Ms. Eberley turned the proceedings over to Acting Chairman Gruenberg for closing remarks.

Closing Remarks

Mr. Gruenberg commented on the value of holding the Committee's meeting in person and expressed favorable sentiments

about the framework that was used for the roundtable discussion. He went on to express his gratitude to the members of the Committee whose terms are expiring - Members Johnson, Lowry, McCurry, Narvaez, Wharton, and Oldner.

There being no further business to discuss, Acting Chairman Gruenberg adjourned the meeting at 2:29 p.m.

Debra A. Decker
Federal Deposit Insurance Corporation
Executive Secretary
and Committee Management Officer
FDIC Advisory Committee on Community Banking

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I hereby certify that, to the best of my knowledge, the attached minutes are accurate and complete.

Martin J. Gruenberg
Chairman
Board of Directors
Federal Deposit Insurance Corporation